Chapter I

RISK MANAGEMENT POLICY

I. Contextualizing Risk Management

As a Digital-Only, first branchless Philippine bank, the Overseas Filipino Bank (OFBank) is mandated to provide competitive and digital products and services through convenient, reliable and secure banking platforms such as:

- Online deposit products and services that are inclusive, accessible and suitable for Overseas Filipinos, Overseas Filipino Workers and their beneficiaries;
- Enhanced credit facilities / financial assistance for OFWs and their families intended to support enterprises development as well as personal needs; and,
- Innovative remittance platform that will strengthen the government's presence in the remittance market and eventually influence lower costs of bank remittance.

However as OFBank continue its digital journey which started with its implementation of online deposit products:

- Digital On-Boarding System with Artificial Intelligence (DOBSAI) - an online account opening facility utilizing artificial intelligence that facilitates an electronic Know-Your-Customer (e-KYC) process;
- iAccess/weAccess/Linkbiz e-banking solutions - safe, fast, easy and efficient electronic services that enable access to bank accounts and carry out online Services such as fund transfers and payments;

Awareness and recognition of the magnitude and intensification of technology risks should correspondingly be more perceptive and discerning. In this networked and market-driven environment, it is critical that OFBank have flexible, adaptable and responsive operating processes as well as sound and robust risk management systems. If not understood and managed properly, these risks may lead to financial losses, business failure or reputational risk.

OFBank's Risk Management (RM) is anchored on its parent bank's (LANDBANK) RM which started as a response to the requirements of the Bangko Sentral ng Pilipinas (BSP) in relation to the implementation of the Basel 2 Accord. As Basel 2 promotes capital adequacy among financing institutions, it prescribes the alignment of capital requirements to the risks of the banks. It emphasizes the practice of risk management in order to better manage capital allocation.

With the Group-Wide Risk Management in place where the risk framework and processes of the parent bank shall apply to all business units in the Group, OFBank's risk management practice shall likewise:

- address existing and potential risks;
- contribute to the achievement of operational efficiencies and good governance;
- act on opportunities for improving productivity and thus, profitability;
- be practiced by all functional units of the Bank, with the risk-taking units or authorized risk takers (ARTs) playing a critical role in the process.

II. Objectives of the Strategic Risk Management Manual

The Strategic Risk Management Manual sets forth OFBank's overall risk management practices, its continuing journey to advanced approaches and its critical role in the Bank's various activities. It hopes to achieve the following objectives:

- Firm up risk management policy and principles of the Bank;
- Document current RM practices into a Risk Management Manual and update subject manual as OFBank's operation progresses **or at least annually;**
- Set forth RM best practices and procedures to facilitate the execution of risk management;
- Clarify roles and responsibilities of OFBank units and how they relate with other in managing risks;
- Provide guidance and ready reference to officers and staff of the Bank;
- Serve as bases for the continual enhancement of RM practices.

III. OFBank's Enterprise Risk Management

Enterprise Risk Management (ERM) is an integrated approach to risk management. It looks at risk from a bank-wide perspective and involves the Board of Directors, Senior Management and all business units in an iterative process of identifying, analyzing, measuring, controlling and monitoring risks. Implementation of the ERM is a transition in the Bank's RM approach, from reactive to proactive.

ERM reinforces risk analysis as it cross-functionally examines interdependencies of risks and dissects its sources. Owing to the wide coverage of participation, it gradually deepens the culture of risk among the officers and staff of the Bank.

IV. Risk Appetite Statement

Risk appetite is the level of enterprise-wide risk that OFBank is willing and capable to manage over an extended period of time. The risk appetite statement of the Bank along with its operating principles and implementing strategies were based on its strategic plan and patterned from the parent bank following the Group-Wide Risk Management protocol.

RISK APPETITE STATEMENT OF OFBANK

Risk Appetite Statement

OFBANK will operate and take calculated risks consistent with its Vision to be the country's leading OFW-centric branchless, digital bank committed to provide competitive and innovative products and services through convenient, reliable and secure banking platforms.

Operating Principle

The Bank shall continue to operate within its area of core competencies while pursuing a balance among its business goals of Pursuit of Mandate, Institutional Viability and Customer Service.

Implementing Strategies

1. The Bank shall continue to take calculated risks to effectively serve its stakeholders, taking into consideration its overall sustainability. The Bank's internal limits shall serve as the management alerts for action.

2. The Bank shall continue to vigorously preserve real capital to sustain business operation in servicing the banking needs of the Overseas Filipinos, the Overseas Filipino Workers and their beneficiaries. Alongside its effort, it will maintain an acceptable annual Return on Equity (ROE).

3. The Bank shall provide innovative financial products and services powered by digital banking platforms where its parent bank possesses expertise and capability to facilitate effective and proactive risk management. When expertise and capability are not yet present, the Bank shall pursue strategic alliances and linkages, acquire talent as well as explore outsourcing with 3rd party providers whose digital platforms/products/services will be jointly evaluated by OFBank and LANDBANK.

4. The bank shall continue to develop long-term relationships with its customers and other stakeholders through strategic alliances and partnerships.

5. The Bank aims to nurture its employees in an enabling environment and provide opportunities for professional growth.

6. The Bank shall leverage on best technology solutions to deliver timely and responsive financial and support services to meet the needs of its clients while promoting sustainable development anchored on good governance.

Explanatory Notes

1. *For the Bank's Risk Appetite Statements (RAS), both quantitative and qualitative approaches were used taking into account several risk appetite dimensions such as the amount of capital supporting risk taking (expressed in CAR) and the acceptable amount of earnings in terms of ROE, among others.*

   The enhanced statements retain the substance of the original RAS crafted by Senior Management.

2. *The Risk Appetite Statements is being reviewed annually during the LBP ICAAP and Recovery Planning process to determine relevance and congruence with LBP Subsidiaries short-term goals and shall be modified based on sound judgment of economic and banking industry situations.*

3. *Core competencies shall refer to all OFBank capabilities expressed in terms of products and services.*

4. *The Capital Adequacy Ratio (CAR) benchmark which is based on the Basel 2 – Pillar 1 prescribed formula, must be revisited periodically.*

5. *The capital adequacy measures the bank's capital and determine the bank's capability to absorb a reasonable amount of losses. The Bank's Capital Adequacy Ratio (CAR) is projected at 59.15% in year 2020 which is way above the required minimum CAR for thrift banks due to increase in the Bank's capital level with the additional infusion from the Land Bank of the Philippines with minimal loan portfolio (risk assets) in the initial year of operations after the closure of branches and transfer of loans to LANDBANK*.

6. *In the medium-term, the Bank shall consider the use of economic capital or modified capital measure as high level expression of its risk appetite.*

7. *New products and services introduced by the Bank should be subject to risk assessment*

V. Risk Universe

OFBank's Risk Universe is a roster of risks that the Bank considers as relevant and is a result of the Risk Self-Assessment (RSA) conducted among top management. The results of the survey questionnaire accomplished by senior officers were further validated through structured executive interviews and meetings to provide context to and firm up selected risks.

OFBank Risk Universe

Credit

Credit Risk Management:
- Credit Concentration Risk
- Contagion Risk
- Prepayment Risk

Liquidity

Capital Reserve:
- Capital Reserve Risk
- Lending Capacity Risk
- Leverage Risk

Liquidity Risk Management:
- Insurance Risk
- Liquidity Risk

Compliance

Compliance Risk Management:
- Compliance Risk
- Related Party Transactions Risk

Code of Conduct:
- Ethics Risk

Legal Risk Management:
- Contract Risk
- Legal Risk

Regulatory:
- Anti-Money Laundering Risk
- Banking Regulations Risk

Market

Market Risk Management:
- Foreign Currency Risk
- Market Risk

Interest Rate

Market Risk Management:
- Interest Rate Risk
  - Basis Risk
  - Model Risk
  - Options Risk
  - Re-pricing Risk
  - Yield Curve Risk

Operational

Accounting and Reporting:
- Accounting, Reporting and Disclosure Risk
- Internal Control Risk

Business Interruption:
- Business Continuity Planning Risk
- Event Risk

Code of Conduct:
- External Fraud Risk
- Internal Fraud Risk

Communications & Investor Relations:
- Employee Communication Risk

Operational

Information Technology:
- Cyber Security Risk
- Data Privacy Risk
- Information Security Risk
- IT Availability/Continuity Risk
- IT Confidentiality Risk
- IT Integrity Risk
- IT Management Risk
- Technology Implementation Risk

People:
- Adequacy of Manpower Complement Risk
- Culture Risk
- Disciplinary Actions Risk
- Performance Management Risk
- Recruitment and Selection Risk
- Remuneration and Compensation
- Separation from Service Risk
- Succession Planning Risk
- Training and Development Risk

Product Delivery:
- Process Risk
- Product Delivery and Support Risk

Product Development:
- Product Creation Risk
- Product Pricing Risk

Sales & Marketing:
- Client Relationship Management Risk
- Marketing Risk
- Sales (Business Growth) Risk

Strategic

Governance:
- Board Performance Risk
- Communication Management Risk
- Tone at the Top Risk

Major Initiatives:
- Measuring and Monitoring of Major Initiatives Risk
- Planning and Execution Risk
- Technology Identification Risk
- Vision and Direction Risk

Market Dynamics:
- Competition Risk
- Socio-Political Risk

Planning and Resource Allocation:
- Forecasting Risk
- Organizational Structure Risk
- Outsourcing Arrangements Risk
- Strategic Planning Risk

Strategic Risk Management:
- Strategic Risk

Reputation

Communication & Investor Relations:
- Crisis Communication Risk
- Customer Suitability / Protection Risk
- Reputation Risk

The Subsidiary Risk Universe which shall be integrated with the LBP Risk Universe shall be formulated as a result of the conduct of RSA.

Guided by the Risk Universe of LANDBANK, risk owners shall be responsible in identifying the risks and risk drivers (what causes risks to happen) through the use of methodologies such as, a.) the Risk Self-Assessment (RSA) survey at the enterprise level and b.) the Risk and Control Self-Assessment (RCSA).

VI. Risk Priorities

There are 21 risks considered as critical to operations in terms of their impact and risk management effectiveness. The 21 critical risks, not in order of criticality, are presented below.

No.	RISKS from the Original Top 19
1.	Liquidity
2.	Capital Reserve
3.	Counterparty Credit Risk: Loans
4.	Market
5.	Client Relationship Management
6.	Banking Regulations
7.	Fraud
8.	Interest Rate
9.	Tone at the Top
10.	IT Management
11.	Recruiting & Retention

No.	Additional RISKS (c/o Steering Committee)
12.	Information Security and Confidentiality
13.	Foreign Currency
14.	IT Availability/Continuity
15.	Lending Capacity
16.	Product Creation
17.	Strategic Planning
18.	Contract Risk
19.	Competition
20.	Lending Capacity
21.	Measurement and Monitoring of Major Initiatives

VII. Risk Dictionary

The Risk Dictionary customizes the definition of the risks that also comprises the parent bank's Risk Universe and was developed by the risk taking units together with the ERM Project Working Committee of LANDBANK and which underwent series of deliberations and were signed-off by the Heads of the concerned operating and support units of LANDBANK.

The Risk Dictionary shall promote a shared understanding of risks within the Bank and its people across the various institutions under the Group-Wide Risk Management.

The risks are categorized according to the eight major classifications prescribed by the Bangko Sentral ng Pilipinas as contained in BSP Circular 510.

Attached as ***Annex A*** is a copy of the Risk Dictionary with updated risk definitions.

Chapter II

CORPORATE GOVERNANCE AND RISK MANAGEMENT COMMITTEE CHARTER

I. Charter of the Corporate Governance and Risk Management Committee (CGRMC) of the Overseas Filipino Bank (OFBank)

A. Overview

Pursuant to Monetary Board Resolution No. 1326 dated August 3, 2017, the Bangko Sentral ng Pilipinas (BSP) issued on August 22, 2017, Circular No. 969, series of 2017 on the revisions to guidelines in strengthening corporate governance for Banks. The amendment requires the establishment of the ***Risk Oversight and Corporate Governance Committee*** under Section 133 of the Manual of Regulations for Banks (MORB):

a) **Corporate Governance Committee (CGC).** *The Corporate Governance Committee shall assist the board of directors in fulfilling its corporate governance responsibilities.*

b) **Risk Oversight Committee (ROC)**. *The ROC shall advise the board of directors on the Bank's overall current and future risk appetite, oversee senior management's adherence to the risk appetite statement, and report on the state of risk culture of the Bank.*

Consistent with this and to address the need for a comprehensive and advanced corporate governance and risk management brought about by industry changes and trends, information technology, banking environment, new products, and other emerging risks, this OFBank **Corporate Governance and Risk Management Committee (CGRMC) Charter** is created. This set the direction for the Committee as well as describe the duties and responsibilities of its members. It shall be approved by the Board and shall be used to guide Committee activities.

This Charter shall be reviewed annually to determine whether its responsibilities are adequately described, and policies are amended, if necessary, in order to adapt to future risks that the Bank may be exposed to.

B. Purpose

This Charter shall serve as the basis for the CGRMC in the performance of its mandated functions. Among others, it provides the composition, authority, duties and responsibilities of the Corporate Governance Committee and Risk Oversight Committee as provided for under BSP Circular No. 969 dated 03 August 2017.

C. Composition

The CGRMC shall be composed of at least three (3) members of the Board of Directors (2 of whom shall be independent Directors, including the chairperson) who shall possess a range of expertise as well as adequate knowledge of the

Bank's risks exposure to be able to develop appropriate strategies for preventing losses and minimizing the impact of losses when they occur.

The following shall be considered in the composition of the Committee members:

1. At least one of the Committee members shall be a member of the Audit Committee;

2. The members shall have no close blood relationship with anyone in senior management of the Bank;

3. The members shall have no close and heavy financial, as well as, business relationship with the Bank, in full compliance with the requirements of existing guidelines such as Code of Ethics, guidelines on Conflict of Interest and rules on Directors, Officers, Stockholders and other Related Interest (DOSRI); and

4. The members shall not be currently, nor have been (in the last three years) employed by the Bank or its Subsidiaries.

   The Board shall appoint the members of the CGRMC. It shall also appoint one of the members as the Chairperson of the Committee.

   More than 50% of the members shall be present to form a quorum.

D. Duties and Responsibilities under Corporate Governance

The CGRMC shall be primarily responsible for:

1. ***Overseeing the nomination process for members of the board of directors and for positions appointed by the board of directors.*** The Committee shall:
   - Review and evaluate the qualifications of all persons nominated to the board of directors as well as those nominated to other positions requiring appointment by the board of directors.
   - Recommend to the board of directors matters pertaining to the assignment to board committees, as well as succession plan for the members of the board of directors and senior management.

2. ***Overseeing the continuing education program for the board of directors.*** The Committee shall:
   - Ensure allocation of sufficient time, budget and other resources for the continuing education of directors, and draw on external expertise as needed.
   - Establish and ensure effective implementation of policy for on-boarding/orientation program for first time directors and annual continuing education for all directors.
3. ***Overseeing the performance evaluation process***. The Committee shall:
   - Oversee the periodic evaluation of contribution and performance (e.g., competence, candor, attendance, preparedness and participation) of the board of directors, board-level committees, and senior management.

4. ***Overseeing the design and operation of the remuneration and other incentives policy***. The Committee shall:
    - Ensure that the remuneration and other incentives policy is aligned with operating and risk culture as well as with the strategic and financial interest of Bank, promotes good performance and convey's acceptable risk-taking behavior defined under its Code of Ethics, and complies with legal and regulatory requirements.

E. Duties and Responsibilities under Risk Management

The CGRMC shall be primarily be responsible for:

1. Fulfilling statutory, fiduciary and regulatory responsibilities.

2. Assisting the Board in defining the risk appetite of the Bank.

3. Ensuring alignment of risk management objectives with overall business strategies and performance goals.

4. Developing and overseeing the risk management programs of the Bank which include the following:

    a. Oversight of management functions and approval of proposals regarding the Bank's policies, procedures and best practices relative to asset and liability management, credit, market and business operational risks ensuring that:

        1) Risk Management systems are in place;

        2) Limits/tolerance levels are observed;

        3) System of limits remain effective; and

        4) Immediate corrective actions are taken whenever limits are breached or whenever necessary.

    b. Ensuring compliance to written policies and procedures relating to the management of risks throughout the Bank. This shall include:

        1) Comprehensive risk management approach;

        2) Detailed structure of limits, guidelines and other parameters used to govern risk-taking units;

        3) Clear delineation of lines of responsibilities for managing risk;

        4) Adequate system for measuring risk; and

        5) Effective internal controls and a comprehensive risk reporting process;

5. Developing a continuing education program to enhance its members' understanding of relevant regulatory and banking industry issues.

F. Specific Duties and Responsibilities

The CGRMC shall perform the following specific duties and responsibilities:

a. The CGRMC shall meet with, request/gather (or compel submission, in proper cases), receive and evaluate information from management and appropriate sources and act or endorse for approval of the Board of Directors, or approve proposals in accordance with its core duties and responsibilities on the following items relating to:

1) Asset and Liability Management

- Fiduciary and asset management activities, including oversight structure for fiduciary activities, general policies and reports;
- Capital allocation methodology;
- Capital levels; and
- Status of the investments and securities portfolio

2) Liquidity Risk

- Liquidity position and liquidity gaps;
- Bank's strategic direction and tolerance for liquidity risk;
- Liquidity risk limits and guidelines;
- Implementation of corrective action in instances of breaches in policies and procedures;
- Contingency plans for dealing with potential temporary and long-term liquidity disruptions; and
- Sufficiency of competent personnel, including internal audit staff, and adequate measurement systems to effectively manage liquidity risk

3) Interest Rate Risk

- Bank's tolerance for interest rate risk/Interest rate risk limits;

- Sensitivity of earnings under varying interest rate scenario;
- Overall interest rate risk profile; and
- Strategies and policies with respect to interest rate risk management

4) Market Risk

- Policies and procedures on market risk, risk measurement methodologies, limit setting, monitoring and control procedures among others;
- Limit setting and ratification of limit structure;
- Market risk resulting from the Bank's trading and information on the "Value-at-risk" calculation models;
- Trends in economy in general with a view of their impact on the Bank; and
- Information relating to compliance with both external and internal regulations regarding market risks.

5) Credit Risk

- Policies and Procedures on credit risk;
- Specific loan portfolios and/or industries;
- Non-performing assets and Real and Other Properties Acquired (ROPA) by the Bank if any, charge-off level and adequacy of the allowance for loan and lease losses;
- Bank's limits on lending, such as industry concentration limits and investing limits; and
- Information relating to compliance with both external and internal regulations regarding credit risks

6) Business Operational Risk

- Policies and procedures on operational risk matters e.g. technology, legal, reputational and personnel risks;

- Management reports relating to operational issues;
- Awareness on proper risk culture and how risks should be addressed; and
- Information relating to compliance with both external and internal regulations regarding operational risks.

b. Promote an enterprise-wide risk culture that requires and encourages the highest standards of ethical behavior by risk management overseers and establish ownership of risks by authorized risk takers;

c. Monitor and evaluate the independence of risk management functions throughout the Bank;

d. Monitor effectiveness of risk management functions, regularly updating the design and operating effectiveness of such controls;

e. Ensure that infrastructure, resources and systems are in place for risk management and are adequate to maintain a satisfactory level of risk management discipline;

f. Review issues raised by internal audit that impact on risk management framework;

g. Meet with, request the submission of and evaluate information from the Management Committee and other committees of the Bank; and perform/approve the necessary actions/proposals as it deems appropriate, regarding the scope of its work, significant findings, together with the actions and responses of management.

h. Oversee the management of future risks rather than risk in past transactions;

i. Recognize those risks and institute contingency plans to mitigate said risks;

j. Provide regular periodic reports to the Board of Directors pertaining to the Bank's overall risk exposure and actions taken to reduce the risks;

k. Encourage the professional development and training of personnel engaged in both risk oversight and risk-taking activities; and

l. Review the effectiveness of the system for monitoring compliance with laws and regulations and the results of management's investigation and follow-up (including disciplinary action) of any instances of noncompliance.

m. Establishes procedures for:

- The receipt, retention, and treatment of complaints received regarding accounting, internal accounting controls;
- The confidential , anonymous, submission by employees of the listed issuer of concerns regarding questionable accounting or auditing matters;
- Reviewing the findings of any examinations by regulatory agencies, and any auditor observations.
- Reviewing the process for communicating the code of conduct to the Bank's personnel, and for monitoring compliance therewith.
- Obtaining regular updates from management and the Bank's legal counsel and other consultants regarding compliance matters.

n. Review and reassess the adequacy of this Charter on an annual basis and recommend any proposed changes to the Board of Directors for approval.

G. Authority

The CGRMC shall exercise authority over matters within the scope of its functions and responsibilities. It is empowered to:

1. Exercise functional supervision over the Central Point of Contact (CPC). Administrative supervision of CPC shall be under the President and CEO;
2. Authorize investigations or verifications into any risk-related matters or obtain any information of the Bank within the Committee's scope of responsibilities.
3. Issue risk management policies and require implementation of Committee instructions and recommendations.

H. Meetings and Procedures

1. The CGRMC shall establish its own rules of procedures consistent with the Bank's Charter and this Charter;
2. The CGRMC shall meet monthly or as often as it considers necessary and appropriate. A majority of the members will constitute a quorum. The CGRMC Chairperson or the majority of its members may call a special meeting when deemed necessary.

An annual calendar shall be prepared to plan meetings, address issues and align with planning and reporting cycles.

3. A notice of each meeting confirming the date, time, venue and agenda shall be forwarded to each member of the Committee at least three (3) working days before the date of the meeting. The notice for members will include relevant supporting papers for the agenda items to be discussed.

4. The Secretariat of the CGRMC shall keep written minutes of its meetings. The minutes and actions taken shall be reported to and noted by the Board.

5. The CGRMC may request any director, officer or employee of the Bank, or other persons whose advice and counsel are sought by the latter, to attend a meeting in order to provide information as it deems necessary.

I. Independence

The CGRMC shall be an independent Committee and for that purpose it shall report directly to the Board of Directors.

J. Effectivity

This Charter shall take effect upon approval.

Chapter III

RISK MANAGEMENT FRAMEWORK

I. The Frameworks

A. Risk Management Framework

Risk Management (RM) is a continuing process of identifying, measuring, controlling and monitoring critical risks across the Bank, in support of its strategic direction and to comply with regulatory requirements as shown in the figure below.

Figure 3.1: Risk Management Framework

The Bank's general RM framework is anchored on sound RM framework implementation which involves the application of the following basic elements which are fundamental in ensuring that risk are effectively identified, measured, monitored and controlled:

- Appropriate Board and Management Committee (ManCom)/Senior management oversight;
- Adequate risk management policies and procedures;
- Appropriate risk measurement, monitoring and control functions; and
- Comprehensive internal controls and independent audits.

The manner of application of these elements in managing various risks will depend upon the complexity and nature of the Bank's risk taking activities as well as on the level of risk exposure.

1. Appropriate Board and Senior Management Oversight

Effective board and Management Committee (ManCom)/senior management oversight of the Bank's various risk activities is critical to a sound risk management process. It is important that the board and ManCom/senior management are aware of their responsibilities with regard to risk management and understand how a specific risk fits within the organization's overall risk management framework.

Responsibilities of the Board of Directors

The Board of Directors has the ultimate responsibility for understanding the nature and the level of risk taken by the Bank. In order to carry out its responsibilities, the Board should:

a. Approve the portfolio objectives, overall strategies, general policies, and ensures that limits are consistent with the Bank's financial condition and risk tolerance. Board-approved objectives, strategies, policies and procedures, and limits shall be documented and clearly communicated to all the personnel involved in their implementation. Changes in strategies and the manner by which investments are managed shall be made under the control of the Bank's appropriate board-level committees.

b. Actively monitor the performance and risk profile of Bank's products/services and risk taking activities against established objectives, strategies and policies and is maintained within tolerance and at prudent levels supported by adequate capital. The members of the board shall act judiciously and shall ensure that bank transactions or business proposals undergo a thorough evaluation process.

c. Ensure that there is an effective management structure and adequate resources for overseeing and conducting all the risk taking activities that enables the achievement of business objectives, strictly enforces controls and implements required independence, check and balance, between different functions consistent with the Group-Wide risk management policy.

Responsibilities of Management Committee (ManCom)/ Senior Management

While the Board gives strategic direction and goals, ManCom/senior management is responsible for implementing board-approved strategic objectives by transforming these directions into procedural guidelines and policy documents and ensure proper implementation of those policies. In managing Bank's activities, it shall have the following responsibilities:

a. Develop and implement policies, procedures and practices that translate the Board's goals, objectives and risk tolerances into operating standards that are well understood by personnel and that are consistent with the Board's intent.

b. Periodically review the organization's RM policies and procedures to ensure that they remain appropriate, sound and consistent with the Board's intent.

c. Ensure adherence to the lines of authority and responsibility that the Board has established for measuring, managing, and reporting the risk exposure in every activities and ensure that personnel involved shall have the requisite technical knowledge and experience.

d. Establish effective internal controls over all RM processes by maintaining appropriate limits structure, adequate systems for measuring risk exposure, and standards for measuring performance.

e. Oversee the implementation and maintenance of risk management information and other systems to identify, measure, monitor, and control the Bank's risk exposure.

f. Ensure that resources are available for identifying, measuring, monitoring and controlling risks

g. Comply with the requirements under the Group-Wide risk management policy.

2. Adequate risk management policies and procedures

The Bank shall institute policies, procedures and limits that provide a framework for managing business activities. The framework for each activity shall be consistent with the Group-Wide risk management policies on business strategies, capital adequacy, technical expertise, and risk tolerance. In setting policies, procedures and limits, the Bank shall be guided by the following:

a. Policies and procedures should clearly articulate guidelines for the conduct of its business activities. The Bank should be able to designate at the onset its specific objective for a particular digital product or service and identify personnel responsible for managing such product or service.

b. Policies should promote the development of a comprehensive understanding of the risks associated with every product/services and activities prior to acquisition and on an ongoing basis. In particular, these should require the following:

1) An appropriate level of due diligence and thorough analysis of the products/services and activities prior to taking a position or implementing a transaction. The depth of the due diligence should depend on the quality, the complexity, and the size of the risk exposure. (i.e., digital products more thorough analyses than traditional products);

2) the analysis to be founded on an analytical review of opportunities, and be sufficient to support a conclusion that the undertaking is sound;

3) the due diligence review to cover:
   a) an analysis of the risks and cash flow characteristics of the specific undertaking, especially for products that the Bangko Sentral ng Pilipinas (BSP) and/or other regulators are yet to define/issue policies on (ie cross border transactions);

   b) an assessment of the valuation and accounting policies to be adopted by the Bank and the extent of its compliance with accounting rules;

   c) an analysis of assumed and actual exit strategies, particularly for products that are not readily marketable, and the resulting effect on earnings; and

   d) the identification of appropriate methodologies for the allocation of capital based on the risk inherent in the Bank's risk taking activities, and the identification of all material risks and their potential impact on the safety and soundness of the institution;

4) periodic and timely reviews of strategies and performance to be conducted at the individual and portfolio levels;

5) the due diligence and ongoing reviews to be performed by qualified personnel or a unit independent from the risk-taking function. Any third-party analysis independent of the seller or counterparty (e.g., reports prepared by investment managers or credit rating agencies) may only be used to complement the Bank's own evaluation. irrespective of any responsibility, legal or otherwise, assumed by a dealer, counterparty, or financial advisor regarding a transaction, the Bank shall ultimately be responsible for understanding and managing the risks of the transaction; and

3. **Appropriate Risk Measurement, Monitoring and Management Information System**

Given the impact of a transaction on the Bank's risk profile, the Bank shall ensure that it has the capability to measure and monitor the risks associated with a product or a transaction prior to acquisition and to be done periodically thereafter. In doing so, the bank| shall be guided by the following:

a. The capability to value positions and measure exposures to each type of risk arising from such positions under both normal and stressed market conditions.

b. The risk measurement system should be able to generate timely information about the market value of assets carried at cost and any significant decline from the carrying value. For this purpose, the Bank shall use reliable data and appropriate tools and metrics that have been properly and independently vetted and approved prior to use.

c. For investments in complex instruments, the Bank shall use more sophisticated tool for identifying, measuring and controlling risks. On the other hand, for investments limited to plain vanilla instruments in the banking book the bank shall, at a minimum, have the capability to periodically mark the positions to market/obtain the market values of their positions.

d. Adopt a proper framework for valuing all positions, including those that are concentrated, less liquid and stale, and make appropriate valuation adjustments for uncertainties in determining the fair value of its assets. The Bank shall likewise establish triggers that would determine whether a presumptive case for challenging the valuation model exists.

e. The valuation methodologies shall be adequately documented. The documentation shall set out the Bank's practices for the initial pricing and marking-to-market/model of its positions. The documentation should also cover model inputs and assumptions, the detail of which would depend on the nature of the financial asset held by Bank and its sources of independent prices.

f. When an incremental change in the value of a position is likely to have a significant effect on the risk profile of the Bank, the Bank is expected to analyze the impact of such change on its overall financial condition.

g. Reports to the Board and ManCom/senior management shall summarize the risks related to the Bank's activities and the performance of portfolios vis-a-vis the established objectives and constraints, as well as any exceptions to established policies, procedures, and limits. Reporting should be frequent enough to provide timely and adequate information and enable the execution of appropriate adjustments to address the changing nature of the Bank's risk profile. The Bank is expected to adjust the frequency of reporting when there are developments that warrant closer monitoring of its positions (e.g., periods of excessive market volatility) and when actions are taken to adjust the level of its exposures.

4. **Comprehensive Internal Risk Controls and Independent Audit (BSP Circular No. 1042, s. of 2019)**

   In addition to complying with the supervisory expectations set out in this manual, the Bank shall:

   a. Adopt internal controls that shall ensure the robustness of the approval process for new products/activities. The Bank shall ensure that the risks involved in new products/activities are fully understood through the implementation of a formal risk assessment program, and that adequate policies, procedures and controls are in place prior to roll out;

   b. Adopt appropriate accounting policies and processes, and maintain adequate records. In this respect, the Bank shall strictly comply with relevant accounting standards and at the same time ensure the consistency of its accounting policies and practices with portfolio objectives and strategies;

   c. Ensure the integrity of valuations, risk measurement methodologies, and controls that address model risk. The valuation process shall be undertaken independently from the risk taking units. New valuation and risk measurement models shall be validated by LBP-Risk Management Group (RMG) prior to use. The models, including any material changes made thereon, shall likewise be periodically reviewed to ensure that they remain fit for their intended use. Model validation processes of a the Bank shall meet the minimum expectations set forth under Guidelines on Market Risk Management and Credit Risk Measurement, Validation and Stress Testing;

   d. Conduct of independent reviews of the risk management system shall likewise be undertaken by the LBP-RMG on a periodic basis, but by no means to exceed three years, to ensure its integrity and reasonableness. These may be in the form of internal or external audits that cover, at a minimum: (a) compliance with and the appropriateness of policies, procedures and limits; (b) propriety of fair valuations and the related processes and controls; and (c) determination of whether the Bank's risk measurement and monitoring systems are commensurate to the nature and complexity of its activities.

B. Input-Output RM Framework

Risk Management is an integral part of the Bank's organizational processes, from planning to performance management, cultivates a well-ingrained risk culture and puts forth opportunities for enhancing income. From an input-output standpoint, the Bank's RM is anchored on the Bank's foundation: its vision, mission and strategies; structure; corporate governance; operating policies and procedures and management systems (Figure 3.2).

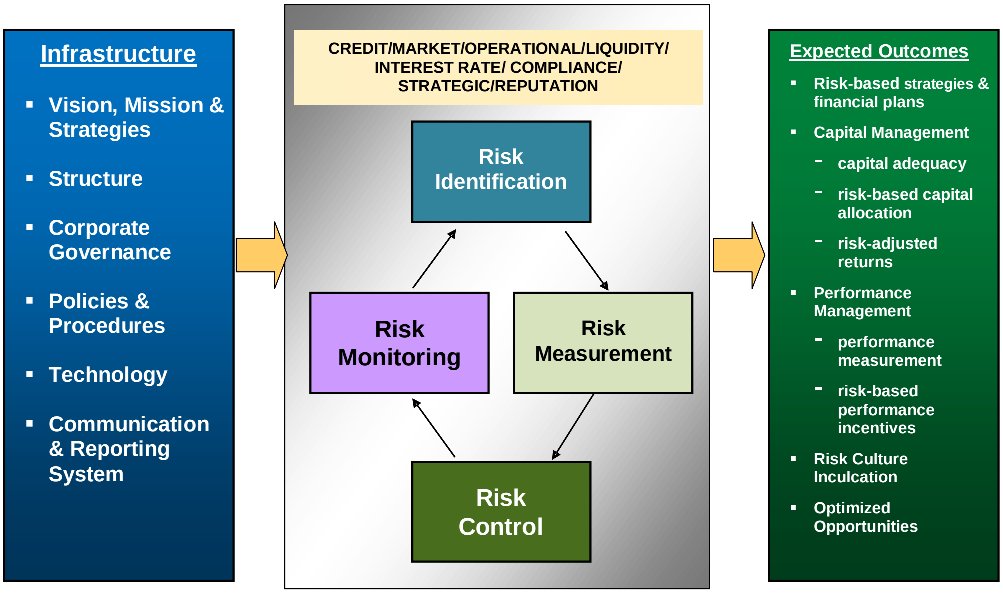


Figure 3.2: Input-Output RM Framework

The Bank's risk-taking activities are aligned with the operating principles and implementing strategies of the risk appetite established by ManCom/senior management.

The expected outcomes from the RM process include risk-based strategies that promote risk-based capital allocation performance management, cultivation of a strong risk culture which optimizes the Bank's business opportunities that ultimately promote capital adequacy and good governance.

RM Implementation Framework

The third framework looks at risk management from a general implementation process viewpoint.

For risk management to be successful and sustainable, it should have the support and strong commitment of the Bank's ManCom/senior management. Management commitment to RM is manifested by: 1.) its articulation and endorsement of the risk management policy; 2.) communicating the benefits of risk management to all stakeholders; 3.) ensuring legal and regulatory compliance and; 4.) ascertaining that the necessary resources are allocated to risk management. Diagram below shows the RM implementation process (Figure 3.3).

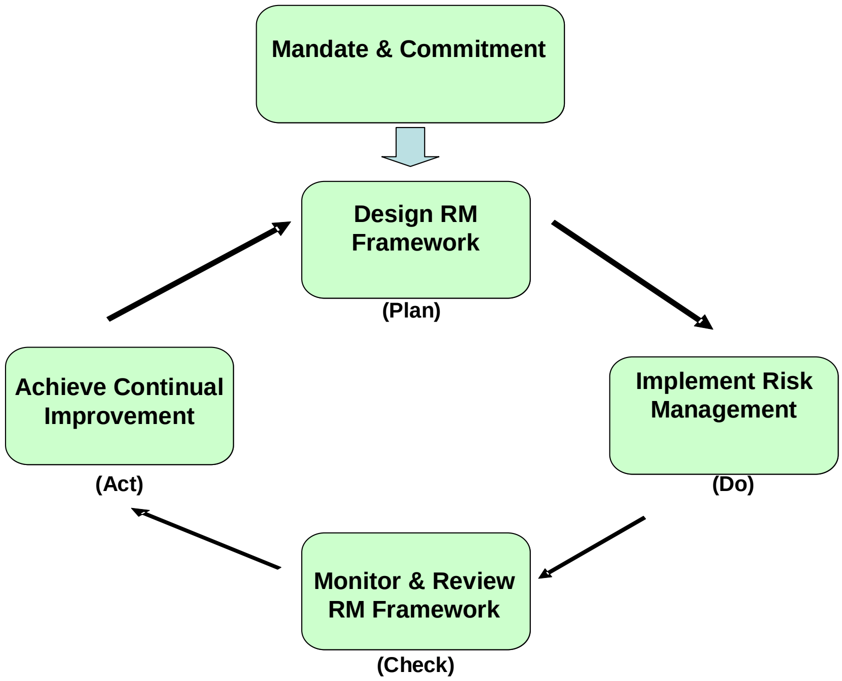


Figure 3.3: Risk Management Implementation Process

1. **Design RM Framework** – the design of the RM framework considers: 1.) the Bank's internal and external environment; 2.) RM policy and commitment to RM; 3.) integration of RM into the Bank' organizational processes; 4.) accountability and authority for managing risks; 5.) resource availability and allocation; 6.) internal communication and reporting mechanisms.

2. **Implement Risk Management** – ascertains that the Bank's risk management process as described in Volume I/Chapter II/ Item II of this manual is applied at all relevant levels and functions of the Bank, as part of its practices and business processes.

3. **Monitor and Review RM Framework** - the Bank: 1.) reviews appropriateness of the RM framework, policy and plan given its external and internal context; 2.) measures progress against the risk management plan; and 3.) reviews effectiveness of the RM process.

4. **Achieve Continual Improvement** - periodic review of the RM framework provides decisions that could lead to enhancements of RM policies, plans and processes. This contributes to improvement in the Bank's resilience, governance and accountability.

C. Risk Management as it Relates to Internal Capital Adequacy and Assessment Process (ICAAP) and Good Governance

The Bank's risk management is a fundamental element of both ICAAP (consolidated with parent bank) and Good Governance. The framework depicts three interrelated and mutually supporting Bank processes, at the core of which is risk management (Figure 3.1)

As a major activity of the ICAAP, risk management pinpoints material risks that could impact on the Bank's capital. RM covers not only the three major risks of the Bank (credit, market and operational) but also includes other risks inherent in all banks (liquidity, interest rate, strategic, reputation, compliance) as prescribed by the BSP. RM acts in synergy with strategic planning and capital management to carry out a risk-based capital adequacy assessment.

In a wider spectrum, risk management endeavors to uphold good governance as it seeks to enhance policies, systems and procedures, as part of the Bank's strategy to address and/or mitigate risks. Risk management assesses adequacy of controls and instills accountability and responsibility.

The interplay of the three processes and the proper functioning of the framework will reduce risk, enhance corporate performance and leadership, improve access to capital and capital adequacy, as well as facilitate compliance to legal and regulatory requirements. Figure below shows the RM, ICAAP & Good Governance Framework (Figure 3.4).

Figure 3.4. RM, ICAAP & Good Governance Framework

D. The Risk Governance Framework

OFBank implements a Risk Governance Framework provided for under BSP Circular No. 971, series of 2017 "Guidelines on Risk Governance". This includes policies which are supported by appropriate processes and control procedures and ensures that risk identification, aggregation, mitigation, and monitoring and communication capabilities are proportionate to the Bank's size, complexity, risk profile, and systemic importance.

Risk Governance Framework shows the risk exposures being addressed through Bank's Enterprise RM process (Processes 1 to 6) that are anchored on the four basic steps of identifying, measuring, controlling and monitoring critical risks across the Bank.

The Bank's risk exposures are adequately managed and mitigated through the active participation of the Board and ManCom/senior management. The RM processes to mitigate and reduce risks are covered by and corresponding policies and guidelines which are in turn implemented at the transactional level of the Business Units (BUs) who are the authorized risk takers.

The Bank's Risk Governance Framework includes as output the Bank's RM tools (e.g., Risk Asset Register/ Risk Treatment Register (RAR/RTR), Business impact Analysis (BIA) Business Continuity Plan (BCP) Credit Rating Systems, Value–at-Risk (VaR) Models, among others. The RM Governance Framework also includes the following;

1. **Risk Appetite Statement** contains the individual and aggregate level and types of risk that the Bank is willing and able to take in pursuit of achieving its business objectives.

2. **RM Policies.** The Bank's RM policies involve the following activities and provisions:

   – Structuring of risk limits and formulation of guidelines to govern risk-taking activities;
   – Delineating responsibilities aligned with the three lines of defense
   – Developing systems for measuring risks;
   – Implementing check and balance system;
   – Establishing framework for data aggregation and risk reporting;
   – Implementing actions taken when risk limits are breached;
   – Notifying, escalating, and reporting of risk limit breaches to Senior Management; and
   – Developing corresponding sanctions for excessive risk taking.

3. **RM Processes and Infrastructure**. The internal control processes and infrastructure are maintained commensurate with developments/ improvements in the Bank. This enables a dynamic, comprehensive, and accurate risk reporting at OFBank level and at the parent bank level critical to the implementation of an enterprise-wide or integrated perspective of risk exposures.

4. **Risk Communication**. The Bank promotes an open communication about risk issues, including risk strategies across the organization.

   The Bank's RM function oversees risk-taking activities, and ensures that the RM activities are within the Bank's risk appetite and in line with the strategic direction.

   In line with this, RMG thru the OFBank Central Point of Contact (CPC) is responsible for facilitating the conduct and implementation of the RM processes, such as identifying, measuring, monitoring and communicating/reporting risks on an enterprise-wide basis. Further, RMG provides assistance to the ManCom/senior management to understand and manage risk exposures, and to direct the implementation of risk policies, processes, and procedures accordingly.

5. **Risk identification, monitoring and controlling** involves the identification and assessment of all material risks including new and emerging risks as well as hard-to-quantify risks. The Bank uses relevant internal and external data and considers the external operating environment in the risk assessment process to identify emerging risks and uses these data to formulate strategic business decisions and RM approaches.

6. **The Bank's Risk Management Process** identifies, measures, controls and oversees risks in all its form. It is both a top-down and a bottom-up process involving the Board of Directors (represented by the CGRMC), the senior management (represented by the Management Committee or ManCom, the business units and the individual Authorized Risk Takers (ARTs). RM process is shown as Figure 3.5. The RM process is composed of the following steps.

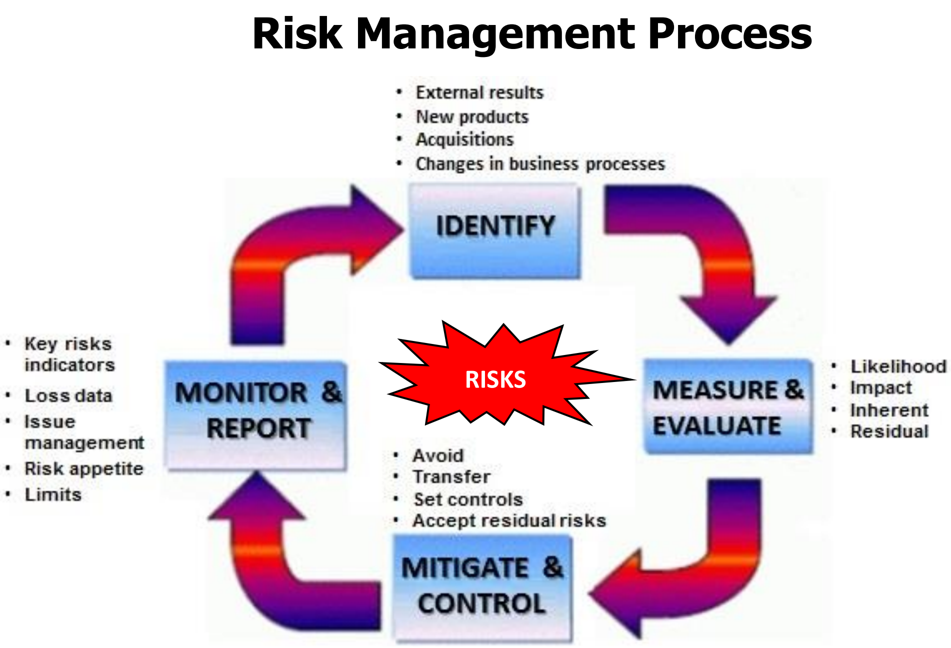


Figure 3.5 Risk Management Process

a. **Risk Identification** is the process of defining, compiling and classifying existing and emerging risks involved in specific business processes. The risks may consist of events and sources of functional and operational problems that could impair the profitability and value of the Bank. In order to arrive at the Bank's risk profile, two general methodologies are used: the Risk Self-Assessment (RSA) at the enterprise level and the Risk and Control Self Assessment (RCSA) at the business unit level.

RSA is the process of assessing the Bank's risks in their purest forms, i.e., without considering controls. In OFBank the RSA is applied as a risk identification and prioritization tool under the Enterprise Risk

Management (ERM). The RSA is a top-down approach that involves the functional unit heads and ManCom/senior management in an iterative process of examining risks the Bank is faced with. The RSA methodology is expounded in Chapter 5 of this volume under ERM.

RCSA, on the other hand, is a structured process of determining risks and examining the effectiveness of controls for such risks at the business unit level, by the authorized risk taker. An important input to the RCSA is the Source Input Process Output Customer (SIPOC) of the business units which provide detailed processes of each Bank transaction and serves as the basis for risk identification. RCSA is a bottom-up approach. The granular risks identified at the transaction level are escalated, validated and aligned with the results of the risks identified under ERM. *Please refer to Volume IV, Chapter 6 for details of the RCSA.*

b. **Risk Measurement** is the process of assessing the magnitude of risks. It involves the Bank's Authorized Risk Takers (ARTs) or risk owners in quantitatively and qualitatively determining the consequences, including financial impact, of possible risk events over a given time horizon under alternative scenarios. The four (4) general types of risk measurement are: Proxy Method, Earnings Volatility Method, Loss Modeling Risk Assessment Method and Direct Estimation Method.

1) **Proxy Method –** a method where the Bank compares itself to similar businesses across the industry by looking at profits, assets and liabilities.

2) **Earnings and Market Volatility Method** – an approach whereby potential earnings are measured against expected and unexpected financial loss.

3) **Loss Modeling Risk Assessment Method** – a procedure that collects actual loss data that is used to predict future losses.

4) **Direct Estimation or Scenario Method –** uses the expertise or judgments of managers on all levels of business to determine real risks.

The risk measurement methodologies being used by the Bank and facilitated by the LBP-RMG are: Value-at-Risk (VaR), Sensitivity Analysis, Stress Testing, Loss Database and Scenario Analysis.

1) **Value-at-Risk** – calculates the maximum loss expected on an investment over a given period of time and given a specific level of confidence. VaR is used for assessing market risk. The Bank computes VaR using a Parametric model with the Bloomberg Portfolio Value-at-Risk (PVaR) function at a 99% confidence interval and daily time horizon. The use of VaR and its importance are explained in detail in Volume 2, Chapter 3 of the Treasury Risk Management manual. VaR falls under the Earnings Volatility Method of risk measurement.

2) **Sensitivity Analysis** – looks into how projected performance varies with changes in the key assumptions which constitute the bases for projections. As a measurement of risk it studies the effect or sensitivity of earnings to assumed changes in inputs, pricing, strategies and other relevant variables. Sensitivity analysis is done by the Bank for both credit and investment portfolios. The uses of sensitivity analysis are elucidated in Volumes 2 and 3 of this manual.

3) **Stress Testing** – a test that measures the stability of a given model and involves verification beyond normal operational capacity to observe results. For instance, the impact on capital and earnings of a huge credit default or a sharp movement in interest rates may be considered.

4) **Loss Database** – is the collection and analysis of loss events and data to enable quantitative modeling and loss prediction of operational risks. Loss database is categorized under Loss Modeling Risk Assessment Method.

5) **Scenario Analysis** – is the process of analyzing possible future events by considering alternative possible situations. It assumes worst-case risk events that could impact on the Bank's earnings and capital.

c. Risk Control is the implementation of measures to reduce risks or to maintain risks within the Bank's risk appetite. It involves the development/ improvement and implementation of policies, systems, procedures and physical changes to address risks. Various risk management options are used to reflect the Bank's actions or responses to risks: Avoid, Retain, Reduce, Transfer and Exploit.

The figure below illustrates various RM options to address/mitigate risks (Figure 3.6).

	AVOID	
* Divest * Target	* Prohibit * Screen	* Stop * Eliminate
	ACCEPT	
* Retain * Self-Insure	* Reprice * Plan	* Offset
	REDUCE	
* Dispense	* Control	
	TRANSFER	
* Insure * Indemnify	* Re-Insure * Scrutinize * Outsource	* Hedge * Share
	EXPLOIT	
* Allocate * Create * Reorganize	* Diversify * Redesign * Arbitrage * Renegotiate	* Expand * Price * Influence

The Risk Control measures are formulated and implemented by the risk-taking units of the Bank.

d. **Risk Monitoring** is the process of tracking and evaluating the performance and status of risk management activities. Risk monitoring is done to determine if:

- risk management strategies or responses crafted have been implemented as planned
- risk action plans are effective in addressing the risks or if new responses should be developed
- risk exposure of the Bank has changed from its prior state and decide on whether risk priorities should be updated
- new risks have occurred that were not previously identified or residual risks are still existing and require new responses
- business assumptions are still valid and if there is a need to revisit and revise the Bank's risk management framework

The products of risk monitoring are various risk reports which are prepared by the CPC in coordination with LBP-RMG and presented to the CGRMC for information, action or approval. Risk reports generated at the operational levels or functional units are escalated to their respective supervisors and presented to the ManCom.

II. Levels of Risk Management

Risk management is performed at three different levels: 1) strategic level; 2) portfolio level; and 3) transactional level. (Figure 3.9)

A. Strategic Level – Risk Policy Formulation and Approval

1) Risk Management at the strategic level generally involves oversight as well as policy formulation and approval. Along the risk and control "lines of defense", this level is ultimately responsible for the effectiveness of risk management activities across the Bank.

2) The highest "line of defense", this level of risk management involves: the Corporate Governance and Risk Management Committee (CGRMC), the Audit Committee (AuditCom) which are board-level committees; and the Management Committee (ManCom).

3) The Board-level committees are responsible for approving the Bank's risk management framework, policies and strategies.

4) ManCom/senior management, on the other hand, identifies, assesses and prioritizes enterprise-wide risks; establishes the risk appetite; and integrates risk

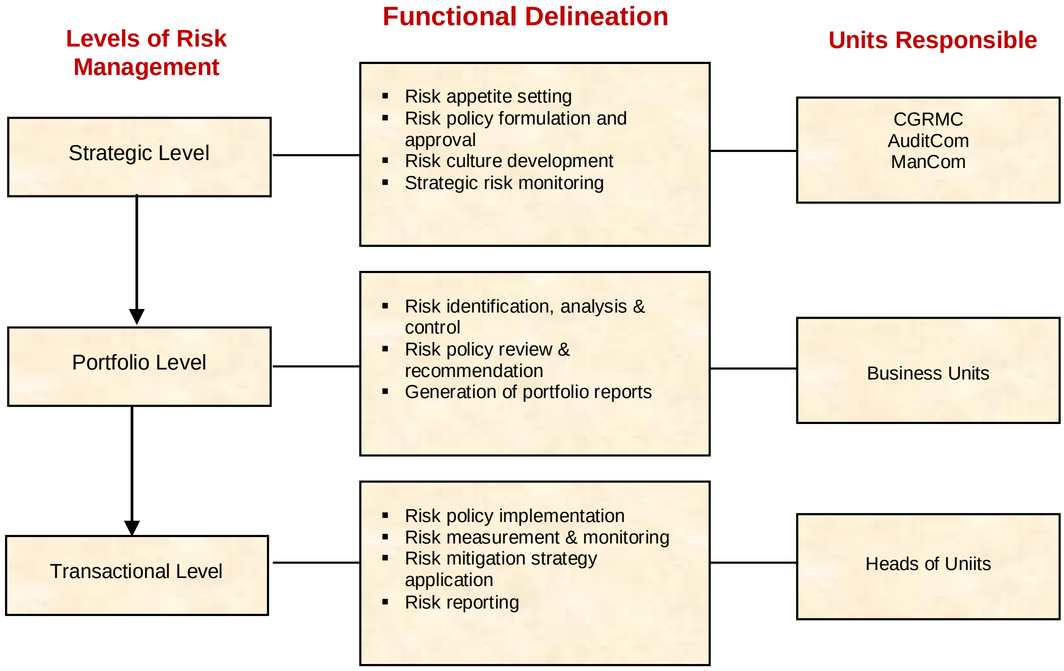
information into its decision-making process to arrive at sound risk management strategies.

5) Both the Board-level committees and ManCom/senior management are responsible for creating a risk culture that promotes a deep sense of risk awareness among the officers and staff of the Bank.

6) Given its oversight function, the LBP-RMG designs and implements the overall risk management framework and provides important inputs in formulating risk management policies.

7) LBP-RMG monitors and analyzes risks from a Group-wide (including LBP subsidiaries) perspectives taking into consideration set risk appetite, tolerances and limits and other relevant risk policies. Policy modifications and enhancements are initiated or recommended by RMG whenever necessary and communicated to the OFBank CPC.

Figure 3.11: LBP Levels of Risk Management



B. Portfolio Level - Analysis, Control and Policy Review

1. Risk management at the portfolio level is the second “line of defense” and is generally responsible for risk analysis, control and management reporting.

2. Portfolio level risk management involves the various units of the Bank the eBusiness Unit, Technology Management Unit, Financial Services Unit, and the Administrative Services Unit.

3. The Heads of each unit are responsible for analyzing and controlling risks under their respective units. They monitor the occurrence of policy breaches and procedural infractions and deviations and ensure that risk measures are properly applied within their own units. Should controls fail in addressing risks, the Regional Heads should review attendant policies and propose workable adjustments when necessary.

4. The CPC collate and consolidate all risk reports from various risk-taking units and prepare the necessary analysis. The consolidated risk reports should then be submitted to the President and CEO and reported to the CGRMC.

5. Portfolio-level risk reports generated by the CPC shall be escalated to the ManCom which shall evaluate performance from a risk-adjusted perspective and to initiate the necessary adjustments in the Bank's overall business strategy and make the necessary proposal to the Board

C. Transactional Level - Implementing Risk Policies

1. The transactional level is the first "line of defense" and is comprised of the business and support units that are directly responsible for the processes and the risks.

2. The transactional level involves specifics of day-to-day risk-taking activities as performed by the risk owners or the Authorized Risk Takers (ARTs). All transactions of ARTs should conform to Bank policies and procedures and should be within specified limits and approving authorities.

3. Identification and recognition of risks and the occurrence of risk events are documented by the ART and reported to the business unit head.

4. Risks are measured and quantified in terms of its impact on the unit's operations and on the targeted revenues.

5. Risk mitigation strategies are applied, whenever possible, to address or resolve the risk event(s).

6. Situations requiring actions by the next higher officer should be escalated by the ARTs in a proper and timely manner.

7. Reports on risk events, policy breaches and procedural infractions and corresponding risk mitigation strategies taken should be elevated to the Group Heads. On a regular basis, risk reports should be prepared and submitted by the risk-taking units to the ManCom and CGRMC.

III. Categories of Bank Risks

The Bangko Sentral ng Pilipinas has identified the major categories of bank risks under BSP Circular No. 510 (Guidelines on Supervision by Risk) as follows:

A. Credit Risk

Credit risk arises from a counterparty's failure to meet the terms of any contract with the Financial Institution (FI) or otherwise perform as agreed. Credit risk is found in all activities where success depends on counterparty, issuer or borrower performance. It arises any time FI funds are extended, committed, invested or otherwise exposed through actual or implied contractual agreements, whether reflected on or off the balance sheet. Credit risk is not limited to the loan portfolio.

B. Market Risk

Market risk is the risk to earnings or capital arising from changes in the value of traded portfolio of financial instruments. This risk arises from market-making, dealing and position-taking in interest rate, foreign exchange, equity and commodities markets.

C. Liquidity Risk

Liquidity risk is the current and prospective risk to earnings or capital arising from an FI's inability to meet its obligations when they come due without incurring unacceptable losses. Liquidity risk includes the inability to manage unplanned decreases or changes in funding sources. Liquidity risk also arises from failure to recognize or address changes in market conditions that affect the ability to liquidate assets quickly and with minimal loss in value.

D. Interest Rate Risks

Interest rate risk is the current and prospective risk to earnings or capital arising from movements in interest rates. Interest rate risk arises from differences between the timing of rate changes and the timing of cash flows (repricing risk); from changing rate relationships among different yield curves affecting FI activities (basis risk); from changing rate relationships across the spectrum of maturities (yield curve risk); and from interest-related options embedded in FI products (options risk).

E. Operational Risks

Operational risk is the current and prospective risk to earnings or capital arising from fraud, error, and the inability to deliver products or services, maintain a competitive position and manage information. Risk is inherent in efforts to gain strategic advantage and in the failure to keep pace with changes in the financial services marketplace. Operational risk is evident in each product and service offered. Operational risk encompasses: product development and delivery, *operational processing, systems development, computing systems, complexity of products and services, and the internal control environment.*

F. Compliance Risks

Compliance risk is the current and prospective risk to earnings or capital arising from violations of, or nonconformance with, laws, rules, regulations, prescribed practices, internal policies and procedures, or ethical standards. Compliance risk also arises in situations where the laws or rules governing certain FI products or activities of the FI's clients may be ambiguous or untested. This risk exposes the FI to fines, payment of damages and the voiding of contracts. Compliance risk can lead to diminished reputation, reduced franchise value, limited business opportunities, reduced expansion potential, and lack of contract enforceability.

G. Reputation Risks

Reputation risk is the current and prospective impact on earnings or capital arising from negative public opinion. This affects the FI's ability to establish new relationships or services or continue servicing existing relationships. This risk may expose the FI to litigation, financial loss, or a decline in its customer base. In extreme cases, FIs that lose their reputation may suffer a run on deposits. Reputation risk exposure is present throughout the organization and requires the responsibility to exercise an abundance of caution in dealing with customers and the community.

H. Strategic Risks

Strategic risk is the current and prospective impact on earnings or capital arising from adverse business decisions, improper implementation of decisions, or lack of responsiveness to industry changes. This risk is a function of the compatibility of an organization's strategic goals, the business strategies developed to achieve those goals, the resources deployed against these goals, and the quality of implementation. The resources needed to carry out business strategies are both tangible and intangible. They include communication channels, operating systems, delivery networks and managerial capacities and capabilities. The organization's internal characteristics must be evaluated against the impact of economic, technological, competitive, regulatory and other environmental changes.

The above definitions were lifted from BSP Circular No. 510. Specific risks recognized by the Bank falling under the above categories and comprising its risk universe are defined in a customized risk dictionary (please refer to Enterprise Risk Management).

IV. Classification of Bank Risks

Risks may be classified as quantifiable and non-quantifiable. Quantifiable risks are those that are subject to numerical measurement through validated methodologies. Thus, they are risks that OFBank should manage and control by means of a structure of general and specific limits. Risk categories falling under this classification are: credit, market, liquidity and interest rate risks. Non-quantifiable risks are risk categories that are not subject to measurement or quantification, but are nonetheless significant and not managed in isolation. These risks have to be identified in all of OFBank's activities and transactions. The table below lists both the quantifiable and non-quantifiable risks of the Bank.

Figure 3.12: LBP Quantifiable and Non-Quantifiable Risks

Quantifiable Risks

Market
- **Currency**
- **Interest Rate**
- **Equity**

Liquidity
- **Funding**
- **Trading**
- **Price/Market**

Credit
- **Direct**
- **Contingent**

Non-Quantifiable Risks

Legal
- **Documentation**
- **Enforceability**
- **Capacity**
- **Bankruptcy**
- **Suitability**
- **Taxation**

Regulatory
- **Monetary Authorities**
- **Tax**
- **Regulatory Bodies**
- **Changing Policies**

Operational
- **Human Factor**
- **Payment Errors**
- **Rate Resets**
- **Position Valuation**
- **P & L Accounting**
- **P & L Reporting**
- **Systems**
- **Modeling Risk**

Personnel
- **Expertise**
- **Fraud**
- **Authorization**
- **Pressure on Profit**
- **Conflict of Interest**

LEILA C. MARTIN
PRESIDENT & CEO
September 3, 2020